

**STATE OF NORTH DAKOTA  
BISMARCK, NORTH DAKOTA**

**REPORT OF EXAMINATION**

**OF**

**LINCOLN MUTUAL LIFE & CASUALTY  
INSURANCE COMPANY  
FARGO, NORTH DAKOTA**

**AS OF  
DECEMBER 31, 2003**

STATE OF NORTH DAKOTA  
DEPARTMENT OF INSURANCE

I, the undersigned, Commissioner of Insurance of the State of North Dakota do hereby certify that I have compared the annexed copy of the Report of Examination of the

**Lincoln Mutual Life & Casualty Insurance Company**

**Fargo, North Dakota**

as of December 31, 2003, with the original on file in this Department and that the same is a correct transcript therefrom and of the whole of said original.

IN WITNESS WHEREOF, I have hereunto  
set my hand and affixed my official seal at my  
office in the City of Bismarck, this \_\_\_\_\_ day of  
\_\_\_\_\_, 2005.

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Jim Poolman  
Commissioner of Insurance

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Fargo, North Dakota  
March 7, 2005

Honorable Alfred W. Gross  
Chair, Financial Condition Committee  
Subcommittee, NAIC  
Commissioner  
Bureau of Insurance  
Commonwealth of Virginia  
P.O. Box 1157  
Richmond, VA 23218

Honorable Jorge Gomez  
Secretary, Midwestern Zone  
Commissioner of Insurance  
State of Wisconsin  
125 South Webster Street  
GEF III – 2<sup>nd</sup> Floor  
Madison, WI 53702

Honorable Jim Poolman  
Commissioner of Insurance  
North Dakota Department of Insurance  
600 East Boulevard  
Bismarck, ND 58505-0320

Dear Commissioners:

Pursuant to your instructions and statutory requirements, a financial examination has been made of the books, records and financial condition of

**Lincoln Mutual Life & Casualty Insurance Company**

**Fargo, North Dakota**

Lincoln Mutual Life & Casualty Insurance Company, hereinafter referred to as the "Company", was last examined as of December 31, 1998, by the North Dakota Insurance Department.

**SCOPE OF EXAMINATION**

This examination was a financial condition examination conducted in accordance with N.D. Cent. Code § 26.1-03-19.3 and observed guidelines and procedures contained in the NAIC *Financial Condition Examiners Handbook*. The examination was conducted to determine the Company's financial condition, its compliance with statutes and to review the corporate affairs and insurance operations. This statutory examination covers the period from January 1, 1999, to and including December 31, 2003, including any material transactions and/or events occurring subsequent to the examination date and noted during the course of this statutory examination.

Work papers provided by the Company's independent auditor, EideBailly LLP, were reviewed and where deemed appropriate certain procedures and conclusions documented in those work papers have been relied upon and copied for inclusion into the working papers for this examination.

All recommendations made in the prior statutory examination report have been adequately addressed by the Company.

This examination was conducted by Examiners from the North Dakota Insurance Department representing the Midwestern Zone.

## **HISTORY**

### **General**

The Company was incorporated on September 13, 1935, under the laws of the State of North Dakota as the "Lincoln Mutual Health and Accident Insurance Association," writing only accident and health insurance.

New Articles of Incorporation and Bylaws were adopted on December 27, 1946, changing the Company's corporate structure to comply with amended Chapter 26-08 of the North Dakota Revised Code of 1943. The Company's name was also changed to "Lincoln Mutual Life and Casualty Insurance Company."

In 1951, the Company acquired the business of the following two entities through merger: Mid-Continental Mutual Life of Minneapolis, Minnesota, and the National United Mutual Life Insurance Company of Fargo, North Dakota. The Company later acquired the Education Mutual Benefit Association of Aberdeen, South Dakota, by means of a 1957 merger.

## **MANAGEMENT AND CONTROL**

### **Membership**

Membership consists of every policyholder insured by the Company or policy owner if different from the primary insured. Each member is entitled to one vote at all annual or special meetings. The annual meeting shall be held on a date in the month of April as determined by the Board of Directors.

### **Board of Directors**

The Bylaws provide that the Board of Directors will be composed of eight persons who will be elected at the annual meeting of the policyholders in such manner as to result in, as nearly as practicable, an equal number to be elected each year. The directors are elected for three-year terms and serve until their successors are elected and qualified.

The annual meeting of the Board of Directors is held immediately after the annual meeting of the policyholders. The dates and time of regular Board meetings are determined by the Directors.

Directors serving at December 31, 2003, were as follows:

**Name and Address**

**Business Affiliations**

Chad S. Niles  
Fargo, ND

Senior Vice President of Marketing  
Noridian Mutual Insurance Company

Robert L. Lamp  
Fargo, ND

President  
Association Services, Inc.

Mark S. Sanford  
Grand Forks, ND

Superintendent of Education  
Grand Forks Public Schools

J. Scott Koltes  
Fargo, ND

Retired President  
Lincoln Mutual Life & Casualty Ins. Co.

Jane M. Bissel  
Valley City, ND

MBO President/CEO  
Catholic Health Initiatives

Richard L. Rayl  
Fargo, ND

Vice President, Finance  
North Dakota State University

Jerome W. Schmidt  
Valley City, ND

President  
Valley Drug

Michael B. Unhjem  
Fargo, ND

President & CEO  
Noridian Mutual Insurance Company

**Officers**

The Bylaws provide that the managing corporate officers shall include a President and Chief Executive Officer, an Executive Vice President, one or more Vice Presidents, a Secretary, a Treasurer, and such other officers as are deemed desirable.

The managing corporate officers serving at December 31, 2003, were as follows:

Michael B. Unhjem  
Lawrence J. Zich  
Chad S. Niles  
Jim A. Austin  
Kim R. Janecky

Chairman of the Board  
President, Treasurer, CFO  
Executive Vice President, COO  
Vice President of Marketing  
Vice President, Secretary

**Committees**

The Bylaws provide that the Company shall have three standing committees: an Executive, Investment and Audit committee. Committee members at December 31, 2003 were as follows:

Executive Committee

Chad S. Niles  
Robert L. Lamp  
Richard L. Rayl  
Lawrence J. Zich  
J. Scott Koltes  
Michael B. Unhjem

Investment Committee

Chad S. Niles  
Jerome W. Schmidt  
Lawrence J. Zich  
J. Scott Koltes  
Michael B. Unhjem

Audit Committee

Mark S. Sanford  
Richard L. Rayl  
Jane M. Bissel

**Conflict of Interest**

The Board of Directors has adopted a policy statement on conflict of interest for disclosure of any possible conflicts. The procedure requires all directors, officers, and responsible employees to annually complete and sign a questionnaire indicating all possible conflicts.

The conflict of interest statements for the years under examination were reviewed and no differences were noted.

**Corporate Records**

The following amendments to the Bylaws were adopted during the period under examination:

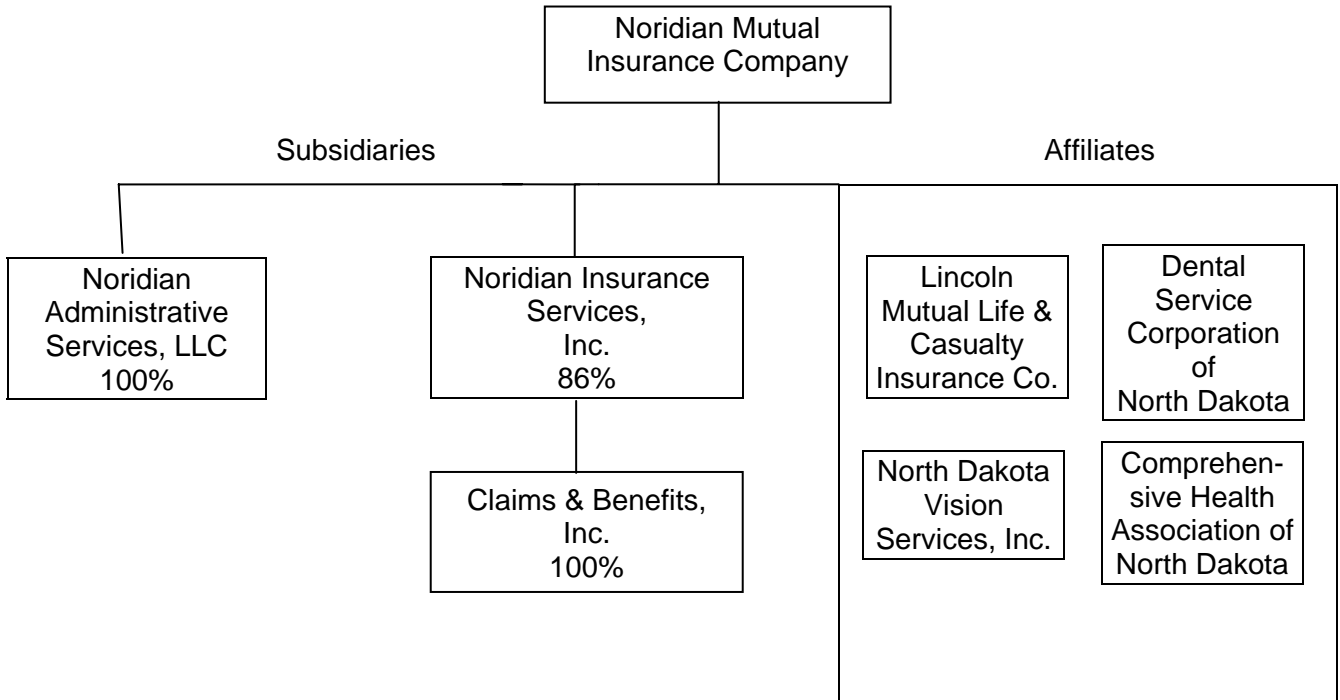
- Article V. Section 1. At its April 12, 1999, meeting the Board of Directors amended the Bylaws reducing the number of Directors from nine persons to eight persons.
- Article VII. Section 1. At its January 29, 2001, meeting the Board of Directors amended the Bylaws to add an Audit Committee to the list of Standing Committees.

**Board of Directors, Policyholders and Committee Minutes**

The minutes of the Board of Directors, policyholders, and committee meetings for the period under examination were read and no exceptions were noted.

## AFFILIATES

The relationship of the Company to Noridian Mutual Insurance Company (Noridian) and its affiliates at December 31, 2003, is shown in the following organizational chart:



As of December 31, 2003, five officers or directors of Noridian were serving on the Company's eight-member Board of Directors and one officer of Noridian was also serving as a Company officer. These individuals are as follows:

<u>Name</u>	<u>LML Position</u>	<u>Noridian Position</u>
Michael B. Unhjem	Director/Chairman of Board	President & CEO
Chad S. Niles	Director, Executive VP & COO	Senior Vice President – Marketing
Jane M. Bissel	Director	Director
Robert L. Lamp	Director	Director
Mark S. Sanford	Director	Director

**Noridian Mutual Insurance Company d/b/a Blue Cross Blue Shield of North Dakota** is incorporated in North Dakota as a nonprofit mutual insurance company and is governed by

Chapter 26.1-12 and Section 26.1-17-33.1 of the North Dakota Century Code. It provides health benefits under contract to subscribers mainly through hospitals and physicians.

**North Dakota Vision Services, Inc. and Dental Service Corporation of North Dakota** are incorporated in North Dakota as nonprofit health service corporations under N.D. Cent. Code Chapter 26.1-17. These entities offer benefits for certain optometric and dental care services to North Dakota subscribers.

**Comprehensive Health Association of North Dakota (CHAND)** was created by the 1981 Legislature to provide comprehensive health insurance to residents of the state who had been denied health insurance or had been given restricted coverage. Noridian Mutual Insurance Company has served as the lead carrier of CHAND since 1983 and performs administrative and claim payment functions for CHAND.

**Noridian Administrative Services, LLC (NAS)** was formed in 2002 to perform Medicare processing functions. NAS has over 1,000 employees and is a wholly-owned subsidiary of Noridian.

**Noridian Insurance Services, Inc. (NISI)** is a subsidiary of Noridian and serves as an insurance agency for Noridian. It provides group life and disability products to the BCBSND sales force. It is 86% owned by Noridian and 14% by the Company.

**Claims and Benefits, Inc.** was formed in 1992 and operates as an insurance agency.

## **AFFILIATE TRANSACTIONS**

### **Facilities Management and Service Agreement**

Under a March 1, 1989, facilities management and service agreement, employees of the Company became employees of Noridian, receiving credit for years of service with the Company in the benefit programs of Noridian. For the year ended December 31, 2003, reported contributions of \$183,865 were made by Noridian to its defined benefit pension plan which contributions are allocable to the Company's operations.

The facilities management and service agreement also provides for Noridian Insurance Services, Inc. (formerly Coordinated Insurance Services, Inc.), a 86% owned subsidiary of Noridian, to perform long-term administration, management, marketing, and insurance services for the Company as directed by the Company's Board of Directors. Compensation for services is based on a cost accounting system which allocates expenses to the Company based on actual utilization. Management fees paid NISI by the Company in 2003 total \$1,637,791.

### **Noridian Insurance Services, Inc.**

Effective January 1, 2003, the Company entered into an agreement with Noridian Insurance Services, Inc. (NISI) for the purpose of appointing NISI as the sole and exclusive agent for the sale of group life and disability insurance in the states of North Dakota and Minnesota. The term of the agreement is from January 1, 2000, until December 31, 2004, and automatically extends thereafter from year to year. The agreement can be terminated by either party by giving the other party at least 90 days advance written notice.



### **Profit Sharing Agreement - Noridian Mutual Insurance Company**

Effective January 1, 2000, the Company entered into a profit sharing agreement with Noridian Mutual Insurance Company (Noridian). The agreement provides for Noridian to receive profit sharing gains from the sale of Company products marketed through NISI, Noridian's subsidiary. The agreement was amended effective January 1, 2003, changing the method used to compute the profit sharing amount. Under the amendment adopted effective January 1, 2003, Noridian's share of the net gains\* are determined in accordance with the following schedule:

Profit up to \$200,000	50%
Profit between \$200,000 - \$400,000	60%
Profit between \$400,001 - \$600,000	70%
Profit between \$600,001 - \$800,000	80%
Profit over \$800,000	90%

- \* If the Company's net income as reported on line 35 of the Company's Annual Statement shows a loss, 25% of Noridian's profit sharing will be forfeited to the Company up to a maximum amount of \$100,000.

The agreement provides for annual settlements which are due within 120 days after the close of each calendar year. Settlements to Noridian under the profit sharing agreement during the period under review were:

2000	\$433,317
2001	\$389,054
2002	\$205,815
2003	\$641,482

## **SERVICE AND MANAGEMENT AGREEMENTS**

### **Group Life Administration and Marketing Agreement**

Under an October 9, 1992, group life administration and marketing agreement between the Company and Pioneer Mutual Life Insurance Company (PML), the Company performs various administrative services relating to group life business that is sold by PML and ceded to the Company under a separate reinsurance agreement. The services performed by the Company include underwriting, policy issue, policy maintenance, policyholder services, claims, premium billing, and agents' training and supervision. Marketing expenses incurred by PML are reimbursed by the Company and PML also receives a share of profits as specified in the agreement.

### **Benefit Plan Administrators**

Effective January 1, 1997, the Company entered into an agreement with Benefit Plan Administrators, Inc. (BPA) under which BPA agrees to provide claim administrative services for the Company. Fees are determined in accordance with scheduled rates and are remitted on a monthly basis.

## FIDELITY BOND AND OTHER INSURANCE

The Company is a named insured on a financial institution bond providing coverage to Noridian Mutual Insurance Company and affiliated companies. The bond specifies a single loss limit of liability in the amount of \$5,000,000 for loss resulting from dishonest or fraudulent acts committed by an employee. The coverage exceeds the minimum amount recommended for the Company and its affiliates in the NAIC's *Financial Examiners Handbook*.

Other insurance coverage covering the Company appeared adequate.

## EMPLOYEE WELFARE AND PENSION PLANS

As noted above, employees of the Company became employees of Noridian pursuant to a March 1, 1989, facilities management and service agreement. Contributions by Noridian to the cost of employee welfare and pension plans are allocable to the Company's operations. The following benefits are available to Noridian employees:

- Group life and accidental death and dismemberment insurance coverage
- Hospital, medical, surgery, vision, and dental insurance coverage
- Retirement benefits through the National Retirement Program of the Blue Cross and Blue Shield Association
- Disability benefits through a national long-term disability program
- Salary savings through a contributory defined contribution plan
- Long term care coverage
- Post employment benefits

## STATUTORY DEPOSITS

The Company maintained the following deposits at December 31, 2003, for the benefit of all policyholders:

Location	Type of Asset	Par Value	Statement Value	Market Value
North Dakota	Bond	\$5,150,000	\$5,165,862	\$5,248,585

Other special deposits at December 31, 2003, are as follows:

Location	Type of Asset	Par Value	Statement Value	Market Value
New Mexico	Bond	\$ 100,000	\$ 100,902	\$ 106,906
Pioneer Mutual Life Insurance Company	Bond	1,185,000	1,183,025	1,299,438
Total		<u>\$1,285,000</u>	<u>\$1,283,927</u>	<u>\$1,406,344</u>

Pursuant to Section 66-2207 of the Arizona Revised Statutes, the Company maintains a permanent guaranty fund of \$500,000 to comply with that state's minimum permanent surplus.

## TERRITORY AND PLAN OF OPERATION

At December 31, 2003, the Company was licensed in 15 states with approximately 96% of its direct business written in the states of North Dakota and South Dakota. States in which the Company is licensed are as follows:

Arizona	Kansas	North Dakota	Utah
Colorado	Minnesota	Oklahoma	Wisconsin
Idaho	Montana	Oregon	Wyoming
Iowa	Nebraska	South Dakota	

The Company's direct business in 2003 consisted primarily of group life and group accident and health and group disability.

The Company had approximately 183 licensed agents at December 31, 2003.

### Growth

Year	Admitted Assets	Total Liabilities	Surplus as Regards Policyholders	Premiums Income	Net Income (Loss)
1998	\$28,567,573	\$23,504,070	\$5,063,503	\$4,927,535	\$935,628
1999	29,568,970	23,633,298	5,935,672	5,533,084	673,456
2000	29,993,041	23,330,044	6,662,997	5,396,371	708,791
2001	29,603,050	22,290,777	7,312,273	5,394,660	687,737
2002	29,563,760	21,758,967	7,804,793	5,565,611	707,072
2003	31,740,952	22,822,423	8,918,529	5,920,546	694,274

1998 and 2003 data was extracted from the prior and current examinations and 1999-2002 data was extracted from the Company's Annual Statements.

## INSURANCE PRODUCTS AND RELATED PRACTICES

The North Dakota Insurance Department has a market conduct staff which performs a review of these areas and issues a separate market conduct report.

### REINSURANCE

The Company's significant reinsurance treaties in force at December 31, 2003, are summarized below.

#### Life and Annuity Reinsurance Ceded:

1.     Type:                   Yearly Renewable Term, automatic and facultative  
  
       Reinsurer:           Swiss Re Life and Health America, Inc.  
  
       Scope:               Group life, accidental death and dismemberment benefits and any disability benefit written supplementary to the life benefit .  
  
       Retention:           Group Life - \$40,000  
                              Group Accidental Death and Dismemberment – 10% of each issue up to a maximum of \$10,000  
  
       Coverage:            Benefits in excess of cedant's maximum limit of retention  
  
       Premium:             Scheduled rates per thousand  
  
       Effective Date:      August 1, 1989  
  
       Termination:         By either party giving 90 days written notice
  
2.     Type:                   Yearly Renewable Term, automatic retrocession  
  
       Reinsurer:           Pioneer Mutual Life Insurance Company  
  
       Scope:               Life insurance amounts at risk on the portion of the original policy reinsured by the Company.  
  
       Retention:           \$30,000 per life for most risks  
  
                              The maximum combined retention of cedant and retrocessionaire: \$200,000, standard to table 4 risks, ages 0-40  
  
       Coverage:            Amounts at risk (i.e., projected death benefit less the projected cash value less the Company's retention) for individual life insurance and supplementary benefits assumed by the Company for business first processed on or after April 1, 1992, on specified plans.

- Premium: Scheduled
- Effective Date: April 1, 1992
- Termination: By either party giving 90 days notice.
3. Type: YRT, automatic and facultative
- Reinsurer: US Able Life Insurance Company
- Scope: Business sold through Coordinated Insurance Services, Inc. in the state of North Dakota, Policy Form VGTL-195, and classified as voluntary group term life and group accidental death and dismemberment issued as a rider to voluntary group term life.
- Retention: Voluntary group term life – 50% of first \$60,000 claims per insured
- Group accidental death & dismemberment - none
- Coverage: Voluntary group term life – 50% of the first \$60,000 claims per insured and 100% of the excess above \$60,000 to a maximum issue amount of \$300,000.
- Group accidental death & dismemberment – 100% of claims per insured up to a maximum of \$300,000 of claims per insured.
- Premium: Scheduled rates per thousand
- Commission: 25%
- Effective Date: July 1, 1995
- Termination: By either party giving 90 days written notice

**Life Reinsurance Assumed:**

1. Type: Coinsurance, automatic
- Cedant: Pioneer Mutual Life Insurance Company
- Scope: Individual life insurance and supplementary benefits including disability waiver of premium and accidental death benefits.
- Retention: None
- Coverage: Risks up to 100% on one life
- Premium: 100% of the gross premium collected.

Effective Date: April 1, 1992  
Termination: By either party giving 90 days written notice by registered letter.

2. Type: Coinsurance, automatic and facultative
- Cedant: Pioneer Mutual Life Insurance Company
- Scope: Group life and group accidental death benefits and dismemberment benefits.
- Retention: Maximum retention is 10% of issue amounts up to \$300,000 per group with employees numbering 501 or more
- Coverage: 90% of indicated risks
- Premium: 90% of the premium on business reinsured under the Agreement
- Other: After ceded business totals \$250,000 of annualized premium, reinsurer pays cedant 25% of net earned premium less: commissions incurred; claim benefits incurred; waiver of premium and conversion charges; general insurance expenses up to 18%; taxes, licenses, fees; and losses carried forward from three preceding accounting periods.
- Effective Date: June 1, 1992
- Termination: By either party giving 90 days written notice

**Accident and Health Reinsurance Ceded:**

1. Type: Coinsurance
- Reinsurer: Noridian Mutual Insurance Company (formerly Blue Cross Blue Shield of North Dakota)
- Scope: All group health policies and Medicare Supplement policies issued in the State of South Dakota.
- Retention: None
- Coverage: 100 percent of the liability for claims and any other benefit under the policies described above
- Premium: 100 percent of the premiums collected less the cost of premium taxes, processing and underwriting applications, billing and collecting premiums from insureds, and receiving processing, adjudicating, and paying claims.
- Effective Date: January 1, 1990

2.	Termination: Type:	By either party giving advance written notice of at least 360 days. Coinsurance, Treaty and Facultative
	Reinsurer:	American Disability Reinsurance Underwriters Syndicate
	Managing Agent:	Integrated Disability Resources
	Scope:	Group long term and short-term disability policies.
	Retention:	Short-term disability – 50% Long-term disability – 0%
	Coverage:	Short-term disability – 50% Long-term disability – 100%
	Premium:	Percentage of premiums received determined for each policy upon reinsurer's acceptance of liability.
	Effective Date:	July 1, 1997
	Termination:	Either party may cancel by written notice received prior to October 1.

All treaties subject to reserve credit limitations contain an insolvency clause as required by N.D. Cent. Code § 26.1-02-21.

## **ACCOUNTS AND RECORDS**

The Company's accounting procedures, internal controls, and transaction cycles were reviewed during the course of the examination and a trial balance as of December 31, 2003, was traced to the appropriate schedules of the Company's 2003 Annual Statement. The Company's ledgers are maintained electronically. Revenues and expenses were test checked to the extent deemed necessary.

The Company is audited annually by an outside firm of independent certified public accountants. The work papers of this firm were made available to the Examiners and were used to the extent deemed appropriate for this examination.

## **FINANCIAL STATEMENTS**

The financial statements of the Company are presented on the following pages in the sequence listed below.

Statement of Assets, Liabilities, Surplus, and Other Funds, December 31, 2003  
Summary of Operations, Year 2003  
Reconciliation of Capital and Surplus, January 1, 1999 through December 31, 2003

**Lincoln Mutual Life & Casualty Insurance Company**  
**Assets**  
**as of December 31, 2003**

	<u>Assets</u>	<u>Nonadmitted Assets</u>	<u>Net Admitted Assets</u>
Bonds	\$25,606,196		\$25,606,196
Stocks:			
Common Stocks	2,590,441		2,590,441
Cash	74,842		74,842
Short-term Investments	1,340,266		1,340,266
Contract Loans	865,102		865,102
Receivable for Securities	11,906		11,906
Investment Income Due and Accrued	389,642		389,642
Premiums and Considerations:			
Uncollected Premiums	(198,583)		(198,583)
Deferred Premiums	146,656		146,656
Reinsurance:			
Amounts Recoverable from Reinsurers	395,500		395,500
Current Federal Income Tax Recoverable	103,726		103,726
Net Deferred Tax Asset	137,772	\$63,320	74,452
Guaranty Funds Receivable or on Deposit	57,609		57,609
Electronic Data Processing Equipment and Software	12,564		12,564
Receivables from Parent, Subsidiaries and Affiliates	22,384		22,384
Other Assets Nonadmitted	4,100	4,100	
Accts. Receivable – STD	15,657		15,657
Accts. Receivable – PML	232,592		232,592
Other Receivables	<u>8,494</u>	<u>8,494</u>	<u>          </u>
Totals	<u>\$31,816,866</u>	<u>\$75,914</u>	<u>\$31,740,952</u>

**Lincoln Mutual Life & Casualty Insurance Company**  
**Liabilities , Surplus, and Other Funds**  
**as of December 31, 2003**

Aggregate Reserve for Life Contracts	\$18,310,807
Aggregate Reserve for Accident and Health Contracts	108,901
Liability for Deposit-Type Contracts	1,799,249
Contract Claims:	
Life	536,367
Accident and Health	114,900
Provision for Policyholders' Dividends Payable in Following Calendar Year:	
Dividends Apportioned for Payment to December 31, 2004	88,500
Premiums and Annuity Considerations Received in Advance	4,106
Interest Maintenance Reserve	361,566
Commissions to Agents Due or Accrued	6,090
Commissions and Exp. Allowances Payable on Rein. Assumed	310
General Expenses Due or Accrued	802,863
Taxes, Licenses, and Fees Due or Accrued	39,226
Current Federal Income Taxes	(32,215)
Unearned Investment Income	17,257
Amounts Withheld or Retained by Company as Agent or Trustee	3,302
Remittances and Items Not Allocated	1,954
Asset Valuation Reserve	543,311
Payable to Parent, Subsidiaries and Affiliates	9,991
Payable for Securities	27,738
Director Fees Deferred	11,262
Interest Due on Policy Funds & Stale Checks	1,270
Accounts Payable PML	2,481
Guaranty Association Liability	<u>63,187</u>
 Total Liabilities	 \$22,822,423
 Permanent Guaranty Fund	 500,000
Unassigned Funds	<u>8,418,529</u>
 Total Surplus	 <u>\$ 8,918,529</u>
 Total Liabilities, and Surplus	 <u><u>\$31,740,952</u></u>

**Lincoln Mutual Life & Casualty Insurance Company**  
**Summary of Operations**  
**for the Year Ended December 31, 2003**

Premiums and Annuity Considerations	\$5,920,546
Net Investment Income	1,490,029
Amortization of Interest Maintenance Reserve	41,781
Commissions and Expense Allowances on Reinsurance Ceded	209,704
Group Experience Refund	111,393
Miscellaneous Income	<u>54,495</u>
<b>Total</b>	<b>\$7,827,948</b>
<b>Deduct:</b>	
Death Benefits	\$2,474,939
Matured Endowments	11,101
Annuity Benefits	77,621
Disability Benefits and Benefits Under Accident and Health Contracts	540,038
Surrender Benefits and Withdrawals for Life Contracts	280,802
Interest and Adjustments on Contract or Deposit-Type Contract Funds	49,865
Payments on Supplementary Contracts with Life Contingencies	1,319
Increase in Aggregate Reserve for Life and Accident and Health Contracts	<u>179,157</u>
<b>Total</b>	<b>\$3,614,842</b>
Commissions on Premiums and Annuity Considerations (Direct)	
765,283	
Commissions and Expense Allowances on Reinsurance Assumed	42,821
General Insurance Expenses	2,328,206
Insurance Taxes, Licenses, and Fees	238,744
Increase in Loading on Deferred and Uncollected Premium	<u>(2,076)</u>
<b>Total</b>	<b>\$6,987,820</b>
Net Gain From Operations Before Dividends to Policyholders and Federal Income Taxes	840,128
Dividends to Policyholders	<u>89,398</u>
Net Gain From Operations After Dividends to Policyholders and Before Federal Income Taxes	\$ 750,730
Federal Income Taxes Incurred	<u>56,455</u>
Net Gain From Operations After Dividends to Policyholders and Federal Income Taxes and Before Realized Capital Gains or (Losses)	\$ 694,275
Net Realized Capital Gains or (Losses)	<u>380,442</u>
<b>Net Income</b>	<b><u>\$1,074,717</u></b>

**Lincoln Mutual Life & Casualty Insurance Company**  
**Reconciliation of Capital and Surplus Account**  
**January 1, 1999, through December 31, 2003**

	<b>2003</b>	<b>2002</b>	<b>2001</b>	<b>2000</b>	<b>1999</b>
Capital and Surplus, December 31, Prior Year	\$7,804,793	\$7,312,273	\$6,662,997	\$5,935,672	\$5,063,503
Net Income	1,074,717	395,564	704,617	896,881	749,372
Change in Net Unrealized Capital Gains (Losses)	369,900	(224,409)	(249,460)	(102,881)	240,202
Change in Net Deferred Income Tax	(36,029)	45,013	(82,276)	0	0
Change in Nonadmitted Assets and Related Items	119,460	(96,920)	(81,123)	592	1,737
Change in Asset Valuation Reserve	(414,312)	373,272	196,170	(67,267)	(160,707)
Cumulative Effect of Changes in Accounting Principles	0	0	161,348	0	0
Change in Federal Income Taxes – Prior Year	0	0	0	0	41,565
Net Change in Capital and Surplus for the Year	<u>1,113,736</u>	<u>492,520</u>	<u>649,276</u>	<u>727,325</u>	<u>872,169</u>
Capital and Surplus, December 31, Current Year	<u>\$8,918,529</u>	<u>\$7,804,793</u>	<u>\$7,312,273</u>	<u>\$6,662,997</u>	<u>\$5,935,672</u>

## COMMENTS ON FINANCIAL STATEMENTS

Financial statement balances at December 31, 2003, are commented upon only if financial changes, recommendations, or special explanations are considered necessary.

### **Bonds**

The Company's custodial agreement with State Bank and Trust does not contain all the provisions required for custody agreements under N.D. Admin. Code § 45-03-23-02.

**It is recommended that the Company pursue changes to its custodial agreement with State Bank and Trust which will bring the agreement into compliance with N.D. Admin. Code § 45-03-23-02.**

The Company did not submit its investment in Noridian Insurance Services, Inc. to the Securities Valuation Office (SVO) as required by the SVO's Purposes and Procedures Manual.

**It is recommended that the Company submit the appropriate filing to the SVO for its unlisted subsidiary, Noridian Insurance Services, Inc., as required by the Purposes and Procedures Manual of the SVO, and in compliance with N.D. Cent. Code § 26.1-03-02.1.**

### **Contract Claims**

The Company's December 31, 2003, reserve for life claims and accident and health claims does not include a component for claim adjustment expenses.

**It is recommended that the Company's claim liabilities for life and accident and health contracts include a component for claim adjustment expenses to comply with SSAP No. 55, paragraph 6, of the NAIC's *Accounting Practices and Procedures Manual*.**

### **Advance Premiums**

Group life premiums are recorded as premium income on the "premium received basis", i.e., premiums are applied (recorded) in the system on the same date or the day after premiums are received. Statutory accounting requires premiums received in advance of the anniversary date to be recorded as advance premiums rather than as premium income.

**In accordance with SSAP No. 51, paragraphs 7 and 25, of the NAIC's *Accounting Practices and Procedures Manual*, it is recommended that the Company record premiums received prior to the reporting date but due after the next anniversary date as a liability for advance premiums rather than as premium income.**

## CONCLUSION

The financial condition of the Company, as of December 31, 2003, as determined by this examination is summarized as follows:

Admitted Assets		<u>\$31,740,952</u>
Total Liabilities	\$22,822,423	
Surplus as Regards Policyholders	<u>8,918,529</u>	
Liabilities, Surplus, and Other Funds		<u>\$31,740,952</u>

No change was made in the amounts reported by the Company in its 2003 annual statement.

Since the last examination conducted as of December 31, 1998, the Company's admitted assets have increased \$3,173,379, its total liabilities have decreased \$681,647, and its surplus as regards policyholders has increased \$3,855,026.

The courteous cooperation extended by the officers and employees of the Company during the course of the examination is gratefully acknowledged.

In addition to the undersigned Examiner In Charge, Rhoda Sautner, CPA, Carole Kessel, CPA, Chief Examiner and Mike Fix, MAAA of the North Dakota Insurance Department participated in this examination.

Respectfully submitted,

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David Weiss, CFE  
State of North Dakota  
Midwestern Zone (III), NAIC

## COMMENTS AND RECOMMENDATIONS

It is recommended that the Company pursue changes to its custodial agreement with State Bank and Trust which will bring the agreement into compliance with N.D. Admin. Code § 45-03-23-02.

It is recommended that the Company submit the appropriate filing to the SVO for its unlisted subsidiary, Noridian Insurance Services, Inc., as required by the Purposes and Procedures Manual of the SVO, and in compliance with N.D. Cent. Code § 26.1-03-02.1.

It is recommended that the Company's claim liabilities for life and accident and health contracts include a component for claim adjustment expenses to comply with SSAP No. 55, paragraph 6, of the NAIC's *Accounting Practices and Procedures Manual*.

It is recommended that the Company record premiums received prior to the reporting date but due after the next anniversary date as a liability for advance premiums rather than as premium income to comply with SSAP No. 51, paragraphs 7 and 25, of the NAIC's *Accounting Practices and Procedures Manual*.